

Aid – development pivot point

A post-World War II invention, development assistance has played a strategic role in advancing standards of living and boosting national economies. It has been used to upgrade social services like education and health, and to develop infrastructure such as roads, railways, ports, telecommunications and power generation – all of which are acquiring added urgency in the current economic downturn.

From the 1950s and for several decades after, resources that flowed from developed countries to the developing world were dominated by “official” – or public sector – financial flows.

The composition of flows from the North to the South during this period was roughly 70 per cent public, 30 per cent private. This ratio in fact formed the basis for the UN target of aid equalling 0.7 per cent of donor country income. For the “development decade” of the 1960s, it was judged that an injection of one per cent of developed country income was needed for economic take-off in the developing world, and therefore 0.7 per cent would have to come from aid, and 0.3 per cent from private investment.

During the globalization phase of the 1990s, however, private investment in emerging markets and the developing world surged, while levels of official development assistance (ODA) stagnated. In less than a decade, the ratio reversed to 30 per cent public versus 70 per cent private. And while during the 1960s donor countries, led by the United States, were investing about 0.5 per cent of national incomes in aid, by the start of the 21st century, the share was down to a bare 0.2 per cent.

Private foreign investment has helped to fuel economic growth in much of the developing world. But public goods in poor countries – public health, education, sanitation and basic physical infrastructure – are generally not attractive to profit-driven investments. Advances in these areas depend on public funding – not only in poor countries, but in all parts of the world. Also, a large number of developing countries lack access to private financial flows, a situation exacerbated by the recent turmoil and resulting risk aversion in credit markets. They continue to rely on ODA to supplement domestic savings in financing investment.

Experience suggests that private and public flows are complementary. ODA is indispensable in preparing the ground for investment and trade opportunities where they are meagre or non-existent, while the income-generating capacity of private investment is a pre-requisite to economic development and higher living standards.

Aid increases and aid gaps

The convening of the International Conference on Financing for Development in 2002 in Monterrey, Mexico, was marked by a general realization among donors that aid levels had fallen too far. Pledges made by the United States and the European Union at this development summit resulted in a sharp increase in ODA levels. By 2005, they surpassed 0.3 per cent of OECD donor country income -- a 50 per cent increase over turn-of-the-century lows, although still falling short of the 0.7 per cent benchmark. Five donor countries – Denmark, Luxembourg, the Netherlands, Norway and Sweden – are notable exceptions, having achieved or surpassed the 0.7 per cent target.

ODA has stagnated at a level slightly above \$100 billion a year since then. The slowdown came after donors had pledged at the 2005 Group of 8 summit in Gleneagles to increase ODA by \$50 billion per year by 2010, to support



achievement of the Millennium Development Goals (MDGs). To meet that commitment, \$18 billion would have to be added to existing flows each year between 2008 and 2010, according to a 2008 report of the UN MDG Gap Task Force. Also behind schedule is progress on the Gleneagles promise to double aid to Africa by 2010.

Gaps in aid effectiveness based on donor-recipient partnership issues also exist:

- Some progress has been made in reducing “tied” aid – which requires that receiving countries spend funds on goods or services of the donor country. But the practice persists, as was recognized at the 2008 High-level Forum on Aid Effectiveness, held in Accra, Ghana, and organized by the Organization for Economic Cooperation and Development (OECD).
- Another way of twisting the purpose of ODA is through excessive conditionality. Conditionality intended to prevent corruption or gross misuse of funds can be overextended into a means of dictating national policies. Intergovernmental talks preparatory to the Doha Review Conference elicited support for the principle that development strategies are to be determined within countries, and not by external conditionalities.
- Questions have also been raised with regard to the practice of channeling ODA through entities other than recipient country governments. While specific situations may require use of NGOs or multilateral organizations as delivery agents of ODA, removing governments from the main share of ODA undercuts the primary objective of developing national capacities and national leadership of development strategies.
- Progress is also required in making aid flows more dependable and predictable, as well as simplifying administration to impose less of a burden on poor countries, according to the OECD. Various analyses also caution of the ability of recipient countries to absorb sudden and uneven increases in aid, as well as potential negative effects on the overall economy of large inflows of ODA.

Non-traditional ODA and innovative sources of finance

While aid increases from the 28 OECD donor countries have stalled, other sources of ODA, although more modest in scale, are rising. Net ODA disbursements by 13 donors that are not members of the OECD’s Development Assistance Committee rose from \$1.5 billion in 2000 to \$5.1 billion in 2006. This figure, moreover, does not include expanding ODA from China and India, much of which is directed to Africa.

Also on the upswing are private contributions. Commitments of private development assistance grew from \$4 billion in 1999 to \$13.7 billion in 2006. This increase was led by new public-private partnerships for health such as GAVI (the Global Alliance for Vaccines and Immunization) and the Global Fund to Fight AIDS, Tuberculosis and Malaria, and by large private donors such as the Bill and Melinda Gates Foundation.

Finally, a number of ideas for new and innovative sources of financing for development either have been proposed or already undertaken. These include:

- The International Finance Facility for Immunization, launched in January 2006, is expected to scale up to \$500 million annually by 2015, through issuance of \$4 billion in floating bonds.
- Air ticket levies, in which 19 countries are involved or are taking initial steps, are estimated to raise between \$1 billion and \$1.5 billion a year in ODA.

All statistics, unless otherwise indicated, are from the Development Assistance Committee of the Organization for Economic Cooperation and Development.